

2012

EXPOSURE DRAFT

GST AND THE SALE OF A CORPORATION'S PROPERTY BY A MORTGAGEE
OR CHARGE

EXPOSURE DRAFT EXPLANATORY MEMORANDUM

Chapter 1

GST and the sale of a corporation's property by a mortgagee or chargee

Outline of chapter

- 1.1 Schedule X amends the *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) to ensure that Division 105 operates to the exclusion of Division 58 in circumstances where a representative of an incapacitated entity is a creditor of the incapacitated entity, and the representative makes a supply in satisfaction of a debt that the incapacitated entity owes to them.
- 1.2 The provisions will take effect from the start of the first quarterly tax period on or after Royal Assent.
- 1.3 All legislative references in this chapter are to the GST Act unless otherwise specified.

Context of amendments

- 1.4 Under Division 105, a creditor is liable for the GST liability on the supply of a debtor's property where the supply is in satisfaction of a debt owed to the creditor.
- 1.5 This means that where a mortgagee in possession or control of a corporation's property exercises its power of sale, the sale of the property by the mortgagee may be a taxable supply under Division 105, even though ownership of the property passes from the mortgagor to the third party purchaser.
- 1.6 In 2008, the Federal Court held in *Deputy Commissioner of Taxation v PM Developments Pty Ltd* [2008] FCA 1886, that the liquidator of an incapacitated entity was not liable for the GST arising from a transaction during the period of the liquidator's appointment. Instead, the Court held that the GST liability is a liability of the company in liquidation.
- 1.7 In response to the decision, the GST Act was amended to insert Division 58 to clarify that a representative of an incapacitated entity is responsible for certain GST consequences which arise from a supply,

acquisition or importation that falls within the scope of the representative's responsibility or authority for managing the incapacitated entity's affairs.

1.8 The definition of 'representative' in section 195-1 was also expanded to ensure that Division 58 would apply to a 'controller' (within the meaning of section 9 of the *Corporations Act 2001*). The definition of 'controller' in the *Corporations Act 2001* includes a person in control or possession of a corporation's property for the purpose of enforcing a mortgage (mortgagee), or a person in control or possession of a corporation's property for the purpose of enforcing a charge (chargee).

1.9 As a result of these amendments, there are circumstances where both Division 58 and Division 105 can apply to a mortgagee or chargee in possession or control of a corporation's property. This gives rise to uncertainty as the two Divisions contain substantially different registration and reporting requirements.

1.10 For example, Division 105 allows a mortgagee to report any GST liabilities arising from the sale of a mortgagor's property under the one GST registration, in the capacity of the mortgagee entity. On the other hand, Division 58 requires a representative to separately register each incapacitated entity that it represents.

1.11 In addition to the different registration requirements, subsection 105-5(3) provides that a supply of a mortgagor's property by a mortgagee in possession or control is not a taxable supply where:

- the mortgagor has provided the mortgagee with written notice that the supply would not be taxable if supplied by the mortgagee; or
- the mortgagee in possession believes that the supply would not be taxable on the basis of reasonable information.

1.12 Division 58 does not provide a similar exclusion.

1.13 The amendments are intended to ensure that Division 105 applies to the exclusion of Division 58 in all cases where a representative makes a supply that is covered by or meets the requirements of paragraph 105-5(1)(a), regardless of whether the supply is taxable or not.

Summary of new law

1.14 Where a representative of an incapacitated entity is in possession or control of the property of a corporation, Division 105 applies to the exclusion of Division 58 to any supplies of property that the representative makes in satisfaction of a debt that the incapacitated entity owes to the representative.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
Division 105 applies to the exclusion of Division 58 to the extent that a representative of an incapacitated entity makes supplies covered by paragraph 105-5(1)(a).	<p>In accordance with the accepted principle of statutory interpretation that a more specific provision applies rather than a more general provision where there is conflict between the provisions, as Division 105 is a more specific provision it applies to the exclusion of the more general Division 58.</p> <p>However, this outcome may not be readily apparent or clear from the current law.</p>

Detailed explanation of new law

1.15 New section 58-95 is inserted into Division 58. Division 58 (including the registration and reporting requirements of Division 58) does not apply to representatives of incapacitated entities to the extent that their supplies would otherwise be of a kind of a supply by a creditor in satisfaction of a debt to which subsection 105-5(1)(a) applies. [*Schedule #, item 2, section 58-95*]

1.16 The insertion of this tie breaker provision means that Division 105 applies to the exclusion of Division 58 in all circumstances where an overlap between Division 58 and Division 105 arises. This ensures certainty for entities engaged in the mortgage lending sector and reduced compliance costs for representatives of incapacitated entities.

Example 1.1

Company MCH borrows money from a finance provider, PLB Bank, to purchase a property. A mortgage is registered over the property with PLB Bank as the mortgagee. The terms and conditions of the mortgage deed allow the mortgagee

to take control or possession of the property and to exercise the power of sale to recover any outstanding debts owed by MCH.

MCH defaults on the loan repayments and PLB Bank takes possession of the property and subsequently exercises its power of sale as mortgagee and sells the property to a third party. The sale proceeds are applied towards the satisfaction of the outstanding debt owed by MCH to PLB Bank. If MCH had sold the property, the sale would have been a taxable supply for GST purposes.

PLB Bank is a controller, as defined in section 9 of the *Corporations Act 2001*, and is therefore a representative, as defined in section 195-1 of the GST Act, for the purposes of Division 58. When PLB Bank sells the property by exercising its power of sale as mortgagee it is making a supply of a kind covered by paragraph 105-5(1)(a).

However, section 58-95 of the GST Act ensures that Division 105 applies to this arrangement to the exclusion of Division 58. More specifically, Division 105 overrides Division 58 to the extent that the representative PLB Bank makes supplies covered by paragraph 105-5(1)(a).

Application provisions

1.1 The amendments contained by this Schedule apply in relation to supplies made on or after the start of the first quarterly tax period starting on or after Royal Assent. [*Schedule #, item 4*]

Consequential amendments

1.2 A note is inserted at the end of Division 58-1 of the GST Act to ensure that Division 58 does not apply to a representative to the extent that paragraph 105-5(1)(a) applies to its supplies. [*Schedule #, item 1, section 58-1*]

1.3 A note is inserted at the end of section 105-1 of the GST Act to clarify that Division 105 overrides Division 58 to the extent that the creditor is a representative of the debtor and the debtor is an incapacitated entity. [*Schedule #, item 3, section 105-1*]